Sheryl P. Walter Declassified/Released US Department of State EO Systematic Review 20 Mar 2014

Message Text

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ACTION SS-25

INFO OCT-01 ISO-00 SSO-00 /026 W
----------110385 150024Z /75
P 142221Z MAR 78
FM AMEMBASSY LIMA
TO SECSTATE WASHDC PRIORITY 9141

C O N F I D E N T I A L LIMA 2247

EXDIS

E.O. 11652: GDS
TAGS: EFIN, PE
SUBJECT: NEXT STEPS BETWEEN THE GOP AND IMF

1. SUMMARY: THE GOP HAS REVISED ITS STRATEGY FOR DEALING WITH THE MF AND IS NOW TRYING TO WORK OUT INTERPRETATIONS OF THE STANBDY AGREEMENT AND/OR ADDITIONAL MEASURES SO AS TO BE ELIGIBILE FOR THE SECOND TRANCHE DRAWING BY LATE APRIL EARLY MAY, THUS OPENING THE WAY FOR PRIVATE BANK LOAN SHORTLY THEREFAFTER, USG DOES NO APPEAR TO HAVE A DIRECT ROLE AT THIS POINT, BUT WE SHOULD TRY TO MAINTAIN A CALM ATMOSPHERE TO GIVE MAXIMUM OPPORTUNITY FOR THE GOP AND THE FUND TO WORK OUT THEIR DIFFERENCES QUIETLY.
END SUMMARY.

2. THE GOP IS TIGHT-LIPPED ABOUT ITS STRATEGY FOR DEALING WITH PROBLEMS THE IMF HAS RAISED IN MEETING STANDBY TARGETS, AND THE GENRAL VIEW IN PRIVATE CIRCLES HERE IS THAT THE GOP IS IN A STATE OF INDECISION AND DRIFT. HOWEVER, WE HAVE BEEN TOLD IN STRICT CONFIDENCE THAT THE SITUTATION IS AS FOLLOWS:

3. THERE ARE THREE POINTS OF DIFFERENCE WITH THE FUND, WHICH THE GOP CONSIDERS MATTERS OF INTERPRETATION OF THE STANDBY AGREEMENT:
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A) RESERVE LEVEL TARGETS. THIS IS A LARGELY TECHNICAL ISSUE OF HOW CERTAIN FINANCIAL BALACES ARE TREATED IN THE CALCULATION OF RESERVE LEVELS.

B) NET BORROWING REQUIREMENT OF PUBLIC SECTOR. THERE WAS A DIFFERENCE OF INTERPRETATION AS TO WHETHER THE ROLLOVER OF THE EIGHT BILLION SOLES VOVIET PAYMENT IN JANUARY COULD PERMIT ADDITIONAL FISCAL DEFICIT ELSEWHERE

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BY THE GOP. APPARENTLY THE GOP HAS ACCEPTED THE IMF VIEW
THAT NO SUCH ADDITIONAL CREDIT IS PERMITTED UNDER THE
FUND AGREEMENT, AND MEASURES ARE BEING DEVELOPED WITHIN
THE GOP TO ADJUST FOR THIS.

C) EXCHANGE RATE. WHILE THE IMF ACCORD PROVIDES
FOR A FLOATING RATE, THE GOP INTERPRETS THIS PROVISION TO
PERMIT TEMPORARY PERIODS OF STABLIZATION OF THE RATE,
WHICH WOULD INCLUDE THE CURRENT ARRANGEMENT AMONG BANKS
TO HOLD THE OFFICIAL RATE AT 130. THE GOP CONSIDERS THE
130 RATE A REASONABLE EQUILIBRIUM LEVEL IF CERTAIN SHORT
TERM FACTORS, SUCH AS BUNCHING OF IMPORT PAYMENTS AND
SPECULATION, CAN BE REVERSED. THE FUND PRESUMABLY WANTS AT
RENEWED FLOAT.

4. THE GOP HAS BEEN WORKING WITH THE FUND (CINCLUDING
THE CONFIDENTIAL VISIT LAST WEEK BY FUND DIRECTOR KAFKA)
TO REACH AGREEMENT ON HOW TO DEAL WITH THESE DIFFERENCES IN
INTERPRETATION. THIS WOULD PRESUMABLY INCLUDE A SCHEDULE FOR
ADDITIONAL FISCAL MEASURES BY THE GOP AND AN UNDERSTAND-
ING ON HOW THE EXCHANGE RATE PROVISION WILL BE IMPLEMENTED
IF THE 130 RATE CONTINUES TO BE AT SUBSTANTIAL VARIANCE
WITH THE HIGHER DOLLAR CERTIFICATE RATE. ACCORDING TO
THE GOP, IT WILL TAKE A MONTH OR MORE TO IMPLEMENT SUCH
AN UNDERSTANDING, WHICH WOULD PERMIT THE GOP TO OBTAIN
THE SECOND TRANCHE OF ITS STANDBY BY THE END OF APRIL
EARLY MAY. THE $260 MILLIONPRIVATE BANK PACKAGE COULD
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BE CONCLUDED SHORTLY THEREAFTER. IN ADDITION, A BRIDGE
LOAN WOULD HAVE TO BE ARRANGED VERY QUICKLY WITH SOME
PRIVATE BANKS TO COVER THE PERIOD FROM NOW UNTIL MAY.
THE BRIDGE LOAN MIGHT BE OBTAINED ON THE BASIS OF AN
AGREED SCHEDULE BETEEN THE GOP AND THE FUND FOR BRINGING
THE GOP INTO COMPLIANCE.

5. COMMENT: THIS TIMETABLE FOR THE SECOND TRANCHE/PRIVATE
BANK LOAN IS CONSIDERABLY EXTENDED FROM WHAT WAS ANTI-
CIPATED ONLY A WEEK OR TWO AGO, AND EVIDENTLY REFLECTS
MORE SERIOUS PROBLEMS ENCOUNTERED WITH THE FUND. THE
GOP VOICES OPTIMISM THAT THE REVISED SCHEULE IS WELL
ON TRACK, BUT THIS MAY MERELY REFLECT THE PERENNIAL
OPTIMISM OF THE GOP IN DIFFICULT SITUATIONS. HOWEVER,
THE UNSUAL DEGREE OF SECRECY THAT PREVAILS BOTH HERE
AND BY THE IMF IN WASHINGTON COULD INDICATE THAT THERE
IS INDEED A SERIOUS ATTEMPT UNDERWAY TO RESOLVE THESE
PROBLEMS. THE FIRST CLEAR INDICATION OF THE OUTCOME MAY
BE WHEN THE GOP SEEKS TO NAIL DOWN A BRIDGE LOAN. PRESUMABLY
LINED TO AN UNDERSTANDING WITH THE FUND THAT
MEASURES WILL BE TAKEN TO MAKE THE GOP ELIBIBILE FOR THE
SECOND IMF TRANCHE BY THE END OF APRIL/EARLY MAY. WE

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DON'T KNOWN HOW CLOSE THE GOP IS TO A LIQUIDITY CRUNCH,
BUT THERE IS MUCH TALK OF SCRAPING THE BOTTOM OF THE
BARREL.

6. THE GOP IS OBVIOUSLY IN A DELICATE POLITICAL SITUATION,
PARTICULARLY IF ADDITIONAL UNPOPULAR FISCAL MEASURES
AND EXCHANGE RATE ADJUSTMENT ARE IN THE OFFERING. THERE IS
A VIEW IN PRIVATE CIRCULES THAT THE GOP SHOULD CHANGEITS
ECONOMIC TEAM AND RENEGOTIATE THE IMF ACCORD. THIS MAY
YET BE THE FINAL RESULT, PARTICULARLY IF BUDGET LEVELS
BECOME A BIGGER PROBLEM THAN THE GOP IS NOW WILLING TO ADMIT.

7. WE HAVE NO APPARENT DIRECT ROLE TO PLAY AT THIS POINT,
BUT WE WHOULD TRY TO MAINTAIN A CALM ATMOSPHERE AND THUS
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GIVE MAXIMUM OPPORTUNITY FOR THE GOP AND THE FUND TO TRY
TO WORK OUT THEIR DIFFERENCES QUIETLY. THE ISSUE
OFNATIONAL SOVEREIGNTY AND PURPORTEDLY UNWARRANTED INTER-
FERENCE BY THE FUND IN INTERNAL PERUVIAN AFFAIRS IS A
CONTINUING PROBLEM FOR PRESIDENT MORALES BERMUDEZ, BOTH
FROM WITHIN HIS GOVERNMENT AND FROM OUTSIDE CRITICS.
IF A COMPROMISE RESOLUTION OF THE BUDGET ANE EXCHANGE
RATE ISSUES CAN BE WORKED OUT BEHIND THE SCENES WITHOUT
APPEARING AS THOUGH THE GOP HAS CAPITULATED FULLY TO THE
FUND, IT WOULD IMPROVE THE POLITICAL CHANCES FOR EFFECTIVE
IMPLENENTATION.
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Message Attributes

Automatic Decaptioning: Z
Capture Date: 01 jan 1994
Channel Indicators: n/a
Current Classification: UNCLASSIFIED
Concepts: NEGOTIATIONS, LOAN AGREEMENTS, IMF DRAWING RIGHTS
Control Number: n/a
Copy: SINGLE
Draft Date: 14 mar 1978
Decaption Date: 20 Mar 2014
Decaption Note: 25 YEAR REVIEW
Disposition Action: RELEASED
Disposition Approved on Date:
Disposition Case Number: n/a
Disposition Comment: 25 YEAR REVIEW
Disposition Date: 20 Mar 2014
Disposition Event:
Disposition History: n/a
Disposition Reason:
Disposition Remarks:
Document Number: 1978LIMA02247
Document Source: CORE
Document Unique ID: 00
Drafter: n/a
Enclosure: n/a
Executive Order: GS
Errors: N/A
Expiration:
Film Number: D780114-0169
Format: TEL
From: LIMA
Handling Restrictions:
Image Path:
ISecure: 1
Legacy Key: link1978/newtext/t19780372/aaaacipr.tel
Line Count: 148
Litigation Code IDs:
Litigation Codes:
Litigation History:
Locator: TEXT ON-LINE, ON MICROFILM
Message ID: 27ebf5c7-c288-dd11-92da-001cc4696bcc
Office: ACTION SS
Original Classification: CONFIDENTIAL
Original Handling Restrictions: EXDIS
Original Previous Classification: n/a
Original Previous Handling Restrictions: n/a
Page Count: 3
Previous Channel Indicators: n/a
Previous Classification: CONFIDENTIAL
Previous Handling Restrictions: EXDIS
Reference: n/a
Retention: 0
Review Action: RELEASED, APPROVED
Review Content Flags:
Review Date: 20 jul 2005
Review Event:
Review Exemptions: n/a
Review Media Identifier:
Review Release Date: n/a
Review Release Event: n/a
Review Transfer Date:
Review Withdrawn Fields: n/a
SAS ID: 3342488
Secure: OPEN
Status: NATIVE
Subject: NEXT STEPS BETWEEN THE GOP AND IMF
TAGS: EFIN, PE, IMF
To: STATE
Type: TE
vdkvgwkey: odbc://SAS/SAS.dbo.SAS_Docs/27ebf5c7-c288-dd11-92da-001cc4696bcc
Review Markings:
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